ACQUIRING OFFICE SPACE FOR STATE AGENCIES - STATUTORY OPTIONS

A Report Prepared for the

Legislative Finance Committee

By

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INTRODUCTION

At its March 2008 meeting, the Legislative Finance Committee heard a report from staff that raised concerns with the processes used to acquire space to house state agency personnel. Of key concern is that the laws that give the Department of Administration authority to allocate space for state government allow the department to enter into long-term leases without any requirements to evaluate if the lease is in the best long-term interest of the state or involve the legislature directly in the long-term funding decisions other than through the temporary general appropriations bill that funds biennium operations of state agencies. Being excluded since 1983 are: 1) a process involving the legislature to evaluate if a state-owned building would save money for the state; and 2) requests for state-owned buildings, even though a 1997 analysis by the Legislative Audit Division determined that building a state-owned building for offices of state agencies would save the state nearly $4.2 million for a 90,000 square foot building with a 40 year useful life over leasing the same space from the private sector.

The committee directed staff to proceed with developing legislative options for requirements that would establish a more formalized structure to evaluate owning against leasing space for state personnel. The committee directed staff to not duplicate, but work with other legislative staff and committees to develop the legislative options for its consideration while minimizing impacts on current interim projects.

LEGISLATIVE CONSIDERATIONS

The legislature may want to consider adding more structure to the direction currently granted to the Department of Administration for allocating facility space for state agencies. The legislature would do so if it is concerned that the current statutory direction provides insufficient structure to adequately ensure that space allocation is controlled in the most cost effective manner and all alternatives are considered in providing facility space when a need arises. The report presented at the March 2008 Legislative Finance Committee meeting[1] identified several concerns the committee concurred in that lead to development of this report.

Many of the actions taken by the State of Washington to provide more accountability, planning, analysis, and reporting could be used by Montana to improve the current requirements for space allocation and address the identified concerns by:

- Requiring a consistent analysis and analysis tool for all lease-versus-own decisions involving building space for state operations
- Requiring long-range planning for building space needs
- Requiring tracking and reporting of building space demographics
- Restricting long-term commitments on leases without legislative involvement

In order to initiate actions to change Montana's space allocation requirements, the committee may want to request a bill for deliberation at its next meeting. However, the committee may want to specify the components of the initial bill draft based on the following decision menu. A motion the committee may consider would be, "to request legislation for enhancing Montana's space allocation laws based on the State of Washington Substitute House Bill 2366 with the following specific requirements [requirements picked for the below menu, including Washington's legislative finding statement]."

THE STATE OF WASHINGTON

To-date, no actions on the office space issues have come out of other legislative committees or their staff. As suggested in committee discussions of the March report, staff has followed the lead of the State of Washington in this regard. Instead of repeating analysis and developing an independent approach to dealing with the issues, the following recommendations are based on actions taken in other states to improve the governance of state facility planning and management.

[1] March report on acquiring office space for state agencies is available at the following Internet location: http://leg.mt.gov/content/publications/fiscal/interim/financecmty_mar2008/Acquiring_Office_space.pdf

During their 2007 regular legislative session, the State of Washington passed Substitute House Bill 2366 (SHB 2366), an act related to accountability, efficiency, and oversight of state facility planning and management. This legislation forms the basis for legislative options for consideration in Montana, because it addresses the same issues and includes key elements for addressing Montana's concerns raised in the March report to the committee. In fact, the Washington legislative findings state that "Capital construction projects funded in the state's capital budget require diligent analysis and approval by the governor and the legislature. In some cases, long-term leases obligate state agencies to a longer financial commitment than some capital construction projects [but] without a comparable level of diligence."

Key Elements of the Washington Legislation

The key elements of the Washington legislation are:

- Development and implementation of a life-cycle cost model required to be used for evaluating space options
- Development of a pre-design process for space requests
- Formalized facility inventories, planning, and reporting
- Restrictions on leasing terms

Life-cycle Cost Model

A requirement was added to the facility management laws to develop and implement a life-cycle cost analysis model for evaluating the costs for owning versus leasing space. The legislation directed the Washington equivalent of the Montana Office of Budget and Program Planning (OBPP) to work in consultation with the appropriate legislative interim committee to prepare an implementation plan for the legislation and to submit the plan to the Governor and that committee roughly two months after the effective date of the legislation. The legislation directed the development, deployment, and periodic update of a life-cycle cost model with development due one year following submission of the implementation plan and included requirements to develop policies, standards, and procedures that specified the following for use of the model:

- When the life-cycle analysis must be used by agencies
- Procedures state agencies must use to document the results of the life-cycle cost analysis
- Standards regarding the discount rate and other key model assumptions
- A process to document and justify any deviation from the standard assumptions

Development of a Modified Pre-design Process for Space Requests

Existing Washington law requires a predesign process for capital construction projects like Montana's Long-range Building Program. A new requirement was added by SHB 2366 for smaller facility projects with estimated project costs less than the $5.0 million threshold for capital projects[2]. The new requirement directs Washington's OBPP to design and implement a modified predesign process for evaluating space requests to lease, purchase, or build facilities involving: 1) housing of new state programs; 2) major expansions of existing state programs; or 3) relocation of state programs. The modified process applies to consolidation of multiple state agency tenants into one facility. Specifics of the predesign process include:

- Agencies perform the modified predesigns and submit them to Washington's OBPP and legislature
- The modified predesigns must include a problem statement, an analysis of alternatives to address the programmatic and space requirements, proposed locations, and a financial assessment[3]
- Proposed projects of more than twenty thousand gross square feel must include a life-cycle cost analysis, but smaller projects only require a cost-benefit analysis
- Planned major facility leases are required to be included in a ten-year capital budget plan

[2] In Montana, state law requires legislative approval for all new buildings costing more than $150,000.

[3] Montana requirements for the Long-range Building Program require an explanation of the problem to be addressed by the proposed project, alternative methods of addressing the problem, the rationale for the selection of a particular alternative, and a projection of increased operating costs incident to the project for the next three biennium.

Formalized Facility Inventories, Planning, and Reporting

Washington added new requirements that directed Washington's OBPP to work with state agencies and Washington's Department of Administration to determine long-term facility needs of state government. A new requirement was to develop and submit a six-year facility plan to the legislature by January 1 of every odd-numbered year starting January 1, 2009. The Washington legislature meets every year but deals with budget matters on the odd years.

Existing Washington law requires Washington's OBPP to develop and maintain an inventory system to account for all owned or leased facilities utilized by state government. A report must be published each year on October 1 that summarizes the information contained in the inventory system. A new requirement directs that the report be submitted to the appropriate fiscal committees of each legislature beginning in 2010. The inventory system must, at a minimum, include the following information for facilities utilized by state government:

- Facility owner (new requirement)
- Location
- Type
- Condition
- Size
- Updated by June 30 each year
- Inventories provided by each agency, department, board, commission, and institution

Upon renewal of any lease, the inception of a new lease, or the purchase of a facility, existing Washington law directs Washington's Department of Administration to determine whether an opportunity exists to consolidate agencies located in the same geographic area into a single facility to improve government efficiency.

A new requirement was added that directs Washington's Department of Administration to report annually to Washington's OBPP and the appropriate fiscal committees of the legislature on facility leases executed for all state agencies for the preceding year, lease terms, and annual lease costs.

Restrictions on Leasing Terms

In addition to increasing the requirements for analysis, planning, and reporting for facility acquisition, Washington placed restrictions on the terms of facility leases. The following lease restrictions were added under SHB 2366:

- Agencies are not allowed to enter into new or renewed lease of more than $1.0 million unless: 1) they have been approved by Washington's OBPP; or 2) the lease is due to an unanticipated emergency, which does not include the regular termination date of an existing lease. If an emergency situation arises, Washington's Department of Administration must notify Washington's OBPP and the appropriate legislative fiscal committees
- State agencies are prohibited from entering into lease agreements for privately owned buildings that are in the planning stage of development or under construction unless there is a prior written approval by the director of Washington's OBPP
- No lease shall extend greater than twenty years in duration
- Director of Washington's Department of Administration shall, on behalf of state agencies, and after consultation with the director of Washington's OBPP purchase, lease, lease purchase, rent, or otherwise acquire all real estate
- The director of Washington's Department of Administration fixes the terms and conditions of each lease agreement but must obtain concurrence from the director of Washington's OBPP for long-term leases greater than ten years, but only after:
    - The OBPP director determines the facility is necessary for the full term of the lease and the lease rate is more favorable than would otherwise be available
    - The director of Washington's Department of Administration determines the life-cycle cost of leasing is less than the life-cycle cost of purchasing or constructing

Menu of Specific Space Allocation Legislation Requirements

Current Statute

Current statutory direction for allocating space in buildings owned or leased by the state specifies that the Department of Administration shall determine the space required by state agencies other that the university system and shall allocate space based on each agency's need. This statutory direction[4] is summarized below.

The department of administration shall determine the space required by state agencies other than the university system, the chambers for the House of Representatives, and chambers of the Senate and shall allocate space in buildings owned or leased by the state, based on each agency's need. The following authority and direction is provided for carrying out this requirement:

- Space should be allocated efficiently and effectively
- The department shall periodically identify the amount, location, and nature of space used by each agency
- The department, in consultation with the agency, shall determine the amount and nature of the space needed
- The department shall locate space within a building owned or leased by the state to meet the agency's requirements
- If space is not available in a building owned or leased by the state, the department shall locate space to be leased in an appropriate building or recommend alternatives to leasing, such as remodeling or exchanging space with another agency
- A state agency may not lease, rent, or purchase property for quarters without prior approval of the department
- For state agencies located in a city other than Helena, the department shall consolidate the offices of these agencies in a single, central location within the city whenever the consolidation would result in a cost savings to the state while permitting sufficient space and facilities for the agencies
- The department may purchase, lease, or acquire, by exchange or otherwise, land and buildings in the city to achieve consolidation
- Offices of the Law Enforcement Services Division and Motor Vehicle Division of the Department Of Justice are exempted from consolidation
- The Department Of Administration may maintain, rent, lease, or construct warehouses

Committee Decisions

The committee may want to consider addressing the following decisions relative to enhancing Montana's space allocation administration:

Decision 1 - Does the committee want to request a bill draft based on the State of Washington model? If this option was chosen, further work on potential costs to implement the changes would be done.

Decision 2 - What does the committee want to apply - all of Washington's requirements or only parts of Washington's requirements? As mentioned above, the key elements of the Washington model are:

- Development and implementation of a life-cycle cost model required to be used for evaluating space options
- Development of a pre-design process for space requests
- Formalized facility inventories, planning, and reporting
- Restrictions on leasing terms

Decision 3 - Does the committee want to also apply requirements that the Washington model does not include?

- Require consideration of communities outside of Helena as an alternative in location planning
- Continue the same exemptions that are currently in the law for university system, the chambers for the House of Representatives, and chambers of the Senate

[4] Space allocation is addressed primarily in 2-17-101 and 2-17-102, MCA

Specifics of Bill Draft

If the committee chooses to enhance the current statutory requirements for space allocation by an affirmative motion on the three of the above decisions specific items that would be included are shown in Appendix A. The requirements are in outline form with the subheadings identifying specific requirements relevant to the higher level requirement. Alternatives considered for each requirement are listed and the staff recommendations that would be included in the initial bill draft are shown in bold. In parenthesis following the staff recommended option is a brief justification for the recommendation.

SUMMARY

At its March 2008 meeting, the Legislative Finance Committee directed staff to work with other legislative committees and staff to develop a decision matrix for legislation to enhance state laws for allocating space used by state government. A menu of legislative decisions is provided that is modeled after actions the State of Washington has taken to address similar issues. Restricting the length of leases and under what conditions the executive can enter into long-term leases, requiring an analysis that compares the cost to lease against the cost for the state to own a facility to meet space needs, and requiring that requests be made of the legislature when owning is determined to be the least cost alternative would improve legislative involvement in the decisions for long-term leasing decisions. Requiring specific long-range planning and reporting for state government space needs would force consideration of alternatives that may improve the efficiency of state government and provide more cost effective alternatives to addressing the space needs without impairing the ability to address the space needs as they arise.

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APPENDIX A

OUTLINE FOR BILL DRAFT BASED ON THE STATE OF WASHINGTON

1. Implementation plan
    - A. Executive agency or program responsible for development
        - i. Department of Administration
        - ii. **Office of Budget and Program Planning** (implementation is statewide and crosses agency boundaries and the office leadership would result in higher lever buy in)
    - B. Legislative committee involvement
        - i. Interim State Administration and Veteran's Affairs
        - ii. Legislative Finance Committee
        - iii. **Interim State Administration and Veteran's Affairs and Legislative Finance Committee** (SAVA has oversight of DOA and LFC provides the fiscal perspective)
    - C. Key implementation deadlines
        - i. Implementation plan submitted to the Governor and legislative committee
            - a. **October 1, 2009** (one quarter year following start of fiscal year of the new biennium)
        - ii. Life-cycle cost model developed, training provided, and implemented[5]
            - a. **April 1, 2010** (six months following implementation plan deadline)
        - iii. Policies, standards, procedures, developed and implemented
            - a. **April 1, 2010** (six months following implementation plan deadline)
2. Life-cycle Cost Model
    - A. Executive agency or program responsible for developing, managing, and updating
        - i. **Department of Administration** (currently responsible for space allocation and Long-range planning program)
        - ii. Office of Budget and Program Planning
    - B. How often do key model assumptions need to be updated?
        - i. Annually
        - ii. **Biennially** (ties to biennial budget cycle)
3. Life-cycle Cost Analysis
    - A. When is the life-cycle cost analysis required to be used?
        - i. **All lease or own decisions** (inclusive and eliminates loopholes of breaking requests into small leases)
        - ii. New leases only
        - iii. New and renewed leases
    - B. Include both the lease and own alternatives in the analysis for what communities?
        - i.. Include only the capitol complex (Capitol Building and all buildings within 10 mile radius of Capitol Building
        - ii. **Require inclusion of other communities in planning and analysis** (legislators indicated strong interest and opportunities for cost savings)

[5] The life-cycle cost model developed in other states, such as Washington, could be obtained and used as a basis for developing Montana's model. This would save time and money.

4. Space needs analysis[6]
   A. Who performs analysis
      i. **Agency identifying the need** (requests are due to agency needs and this would spread the workload)
      ii. Department of Administration
   B. Required for what space needs requests?
      i. Space for new state program
      ii. Space for major expansion of existing state program
      iii. Space for relocation of existing state program
      iv. All the above purposes only (Washington model)
      v. **All space need requests** (maximize opportunities to provide savings and supporting information, also eliminate loopholes)
   C. Minimum components of the space needs analysis (minimum to provide good analysis)
      i. **Problem statement**
      ii. **Analysis of alternatives to address the programmatic and space requirements including evaluation of relocating operations in other communities as appropriate**
      iii. **Life-cycle cost analysis of all alternatives**
      iv. **Programmatic impact analysis of proposed alternatives**
   D. Reporting requirements
      i. Provide analysis report only to the Department of Administration
      ii. Provide analysis report to the Department of Administration and the Office of Budget and Program Planning
      iii. **Provide analysis report to the Department of Administration, the Office of Budget and Program Planning, and the Legislative Fiscal Analyst** (OBPP – statewide oversight and awareness, LFA – use in analysis and clearinghouse for legislator information)
5. Formalized space and facility inventory, planning, and reporting
   A. Require long-range space needs planning including alternatives to address the space needs identified
      i. For the current through the next biennium
      ii. **For the current and through the next two biennia** (provide realistic forecasting window for needs and ties to funding and construction cycles if state ownership is lowest cost alternative)
      iii. Ten years out
   B. Facilities to be included in space need planning (inclusive of likely alternatives)
      i. **Lease retirement/renewal (as determined by life-cycle cost analysis)**
      ii. **Agency consolidations**
      iii. **State building construction or purchase**
6. Inventory of owned or leased facilities utilized by state government
   A. Who should be responsible for the statewide inventory system?
      i. **Department of Administration** (currently responsible for allocating space)
      ii. Office of Budget and Program Planning
   B. Who collects inventory information during updates
      i. **Tenant agencies based on guidelines from the Department of Administration** (space needs are due to agency needs, they are the tenants and are the signers of the leases if space is leased)
      ii. Department of Administration

[6] In Washington, the threshold for capital projects to be included in what is Montana's Long-Range Building Program is buildings costing $5.0 million or more. In Montana, state law requires legislative approval for all new buildings costing more than $150,000. The Washington modified predesign process was changed to a space needs analysis with the same required components of the Washington modified predesign process.

- C. Minimum information in inventory system (minimum information to be useful)
  - i. **Facility owned by**
  - ii. **Location**
  - iii. **Type**
  - iv. **Condition**
  - v. **Size**
  - vi**.** **FTE limit and currently being housed**
  - vii. **Age, if owned, or lease end date**
  - viii. **Annual lease cost or ownership cost if owned**
- D. Inventory updated
  - i. **By January 1 each year** (available for the legislature and the beginning of the budget cycle)

7. Space needs plan and inventory summary report
- A. Reports provided to
  - i. **Office of Budget and Program Planning** statewide oversight and awareness)
  - ii. **Legislative Fiscal Analyst** (use in analysis and clearinghouse for legislator information)
- B. Report provided by
  - i. **March of each even year** (consistent with the start of the budget cycle)
- C. Leases included as a part of the Long-range Building Program request to the legislature
  - i. Leases for 5 years or more
  - ii. **Leases for 10 years or more** (threshold for DOA approval without concurrence of OBPP if the legislature didn't approve funding when previously requested)
  - iii. Leases for 20 years or more
  - iv. Leases for 30 years or more
- D. Annual report on new leases executed in previous year with lease terms and annual lease cost
  - i. **September 1 to Office of Program Planning and Legislative Fiscal Analyst** (two months after the end of each fiscal year)

8. Restrictions on lease terms for new and renewed leases without prior legislative approval
- A. Limit lease length if a life-cycle cost analysis determines leasing is more costly than state ownership
  - i. Lease term for new or renewed leases may not extend beyond the current biennium and a building request shall be included in the Long-range Building Program request to the next legislature
  - ii. Lease term for new or renewed leases may not extend beyond the current biennium plus two fiscal years and a building request shall be included in the Long-range Building Program request to the next legislature
  - iii. Lease term for new or renewed leases may not extend beyond the current biennium, an unanticipated emergency exists[7], and a building request shall be included in the Long-range Building Program request to the next legislature
  - iv. **Lease term for new or renewed leases may not extend beyond the current biennium plus two fiscal years, an unanticipated emergency exists, and a building request shall be included in the Long-range Building Program request to the next legislature** (allows short-term leases to meet unanticipated needs while funding is requested of the legislature, also allows two years to design and construct a building if funding is provided by the legislature)

[7] An unanticipated emergency does not include the regular termination of an existing lease.

B. Limit lease length if a life-cycle cost analysis determines leasing is less costly than state ownership
   i. No leases longer than
      a. **20 years** (limits long-term commitment on leases)
   ii. Approval of the director of the Department of Administration
      a. **10 years and previous legislature disapproved a request for a state building** (limits long-term commitment without additional oversight by OBPP)
   iii. Approval of the director of the Department of Administration with concurrence of the budget director
      a. **20 years, the previous legislature disapproved a request for a state building, and the budget director determines: 1) the facility is necessary for the full term of the lease; and 2) the longer term lease is more favorable than would otherwise be available under a shorter lease term** (allows option to save funds if longer term provides it while limiting long-term obligation of the state)

C. **Prohibit entering into lease agreements for privately owned buildings that are in the planning stage of development or under construction unless approved by the budget director.** (additional level of oversight and accountability)

9. Exceptions
   A. **Continue the current exceptions for the university system, the chambers for the House of Representatives, and chambers of the Senate** (separations of powers)